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## THE PROTECTION OF MUNICIPAL BONDS

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A very little investigation of the manner in which municipal bonds are ordinarily issued will reveal a condition wherein the crime of forgery might find its natural domicile. It is not a matter for wonderment that bonds of this class are so frequently forged, but rather that an opportunity so ready and with such large possibilities of easy pecuniary gain should be comparatively neglected by those whose business daily brings them into close touch with the situation.

In providing a corrective for any defective condition it is desirable first to become familiar not only with the actual condition to be remedied but also with the underlying causes which have contributed to the fault. When these are not known, or but imperfectly appreciated, the well-meant labor of those who would afford relief is not only ineffective but tends to bring about a state of greater confusion and also to produce in the public mind an impression that no adequate remedy can be found. It is, however, unnecessary for our purpose to trace the history of the municipal bond from its beginning as a simple written order to be immediately paid out of funds in hand through its various stages of growth as a warrant without fixed maturity bearing interest until paid, to a bond with or without interest coupons attached and becoming due at a stated time. A few points only may be noted.

In 1883 the business of handling municipal bonds had grown to such considerable proportions that many large firms with adequate capital were engaged almost exclusively in buying and selling this class of securities. Since that date the annual output of municipal bonds has increased enormously, and now reaches a total of about half a billion dollars.

The necessity for providing a safe bond was not at first appreciated by municipal officials. Not infrequently bonds that were typewritten, printed or otherwise cheaply prepared would be tendered to purchasers; therefore, in order to obtain bonds which were businesslike in appearance and acceptable to their clients,

dealers found it necessary to furnish the blanks to the municipalities. This procedure eventually became a source of much trouble, for while the honest dealer could, in a measure, protect himself and his clients, those less scrupulous found in the practice an easy way to increase their capital.

Dealers in municipal bonds are justly held in high esteem as men engaged in an honorable business, requiring a capital large in proportion to the returns to be expected from its ordinary transactions. They must also, in order to do business at all, command the respect and confidence of the most cautious and conservative investors, for to such the bulk of municipal bonds are finally sold. When, therefore, men of such high standing yield to temptation and are false to the trust reposed in them, it must make thinking men pause and ask why this business, which should be absolutely free from even liability to suspicion, is not surrounded with such safeguards as to afford practical protection to those engaged in it, and to their clients.

From the first, abuses existed, such as over-issues, duplicates and actual forgeries, beginning in a small way, then increasing with the growth of the business until recently a single individual using the credit of his firm issued forged municipal bonds having an ostensible par value of over a million dollars. An evil of such magnitude naturally attracted public attention, and various attempts have been made by state legislators to surround the issue of bonds with formalities intended to prevent such irregularities as have been mentioned.

The various expedients adopted by dealers and by the various state legislatures, while tending to reduce the chances of the bonds being improperly executed or issued in excess of the amount authorized, however, protect only in part, and even when working together do not constitute an effective plan for the purpose, which should be to provide a bond itself bearing indubitable evidence of its own genuineness, a difficult task, but not impossible of accomplishment.

To meet such difficult conditions, to safeguard the issuing municipality, the dealer, the banker loaning on bonds as collateral, and the investor, against loss through accidental over-issue or subsequent fraudulent duplication, the method of issue must be at once economical, comprehensive, and exact in every detail; and the finished bond must be such that to the careful observer there can

be no doubt of its genuineness. In short, the bond itself should provide its own identification with even more certainty than does a treasury note or bank bill.

For some years the United States Government has safeguarded its bond issues by having the blanks prepared at the Bureau of Engraving and Printing under a checking system which has proved effective against liability to over-issue. Immunity from counterfeiting is secured by the use of a special paper and elaborate engraving, both plates and designs being further protected by heavy penalties attached to their possession or use by unauthorized persons. These expensive and elaborate precautionary measures were not adopted needlessly, but because experience has shown that the most perfect system was required to discourage would-be counterfeiters.

Several of the larger cities have attempted to meet the emergency by providing steel plates engraved by bank note companies, from which their bonds are printed. The smaller municipalities, however, are unable to afford even this partial remedy because of the expense attending not only the original engraving, but the changes in the text of the bonds necessary to provide for successive issues. As it is evident that the most careful engraving will not of itself be sufficient and that mere registration by state officials cannot prevent forgery, the remedy must lie in a complete system of issue providing for exacting supervision of every detail, all under the direction of a responsible and permanent corporation, which will affix to each bond an absolute guarantee of its genuineness.

In the issue of corporation bonds, it has long been the custom to require that identification be furnished by means of a certificate endorsed on each bond signed by a trustee (usually a trust company) before it becomes a valid obligation of the issuing corporation, but as the certificate also may be forged the evidence of genuineness is not so sufficiently conclusive that the purchaser does not still have to depend on the word of the vendor for his assurance that the bond is what it purposes to be.

As in the case of corporation bonds, a responsible and conservative trust company would seem to be the proper sponsor for municipal obligations, and as the trust company must first assure itself against accidents it must control all the details of manufacture from the time the paper leaves the vat, through all the various

processes, until the bonds are sealed, signed, attested by certificate and delivered.

The physical protection of the issue should be as perfect as the present state of the several arts employed will permit—thus, the paper should be made from a special formula and bear a distinctive watermark. Provision should be made whereby every sheet of the paper may at all times be accounted for until it is in the form of a completed bond. The engraving used should be of a character most difficult and costly to reproduce, and the plates should be owned by the trust company, which should also own the designs from which the plates were engraved, as otherwise they might be employed for other purposes and their value as a protective feature entirely lost. When the exact number of bonds required has been prepared and they have been executed under the direction of a responsible representative of the trust company who has first ascertained that the parties signing were the proper officers of the municipality, they are ready for the signing of the certificate of genuineness, which should be a full and explicit guarantee of the genuineness of the signatures and the seal attached to the bonds. Affidavits as to the proper execution of the bonds acknowledged by both the officials and the trust company's representative should then be filed for future reference and the bonds delivered.

In the space of this article it would be impossible to give more than a short reference to the conditions which have made a protective method of issue necessary and a brief general statement of the essential features of such a method without going into the almost innumerable details of which the method is composed. The painstaking care and exacting supervision which those details require in order to make the plan effective may also be passed without further mention. Taken as a whole the plan outlined is, under experienced direction, a success, and has been operating long enough to prove its practical value to municipalities desiring to safeguard the interests of the taxpayer and to the more conservative investors who appreciate the security thereby afforded to their investments.